

MINUTES

MONTANA SENATE 57th LEGISLATURE - REGULAR SESSION COMMITTEE ON TAXATION

Call to Order: By **VICE CHAIRMAN ALVIN ELLIS**, on February 16,
2001 at 8:00 A.M., in Room 405 Capitol.

ROLL CALL

Members Present:

Sen. Bob DePratu, Chairman (R)
Sen. Alvin Ellis Jr., Vice Chairman (R)
Sen. John C. Bohlinger (R)
Sen. Mack Cole (R)
Sen. Pete Ekegren (R)
Sen. Jon Ellingson (D)
Sen. Bill Glaser (R)
Sen. Dan Harrington (D)
Sen. Emily Stonington (D)

Members Excused: None.

Members Absent: None.

Staff Present: Lee Heiman, Legislative Branch
Deb Thompson, Committee Secretary

Please Note: These are summary minutes. Testimony and
discussion are paraphrased and condensed.

Committee Business Summary:

Hearing(s) & Date(s) Posted: SENATE BILL 446, 2/13/2001
Executive Action: None

HEARING ON SENATE BILL 446

Sponsor: SENATOR BOB DEPRATU, SD 40, Whitefish

Proponents: Mike Uda, Energy Northwest; Chris Byrd, President of
E&I; Francis Rosse, Flathead Electric; Joe Unterreiner, Kalispell
Chamber of Commerce; Warren McConkey, Flathead Electric

Opponents: Tom Harrison, representing Spring Creek Coal

Opening Statement by Sponsor: SENATOR BOB DEPRATU presented the bill. He explained SB 325 dealt with enabling electric cooperatives. SB 446 was considered a backup bill to that. The situation in Kalispell was the co-op bought out PP&L properties, which is now called Energy Northwest. That company is now part of the co-op but the enabling legislation is needed to allow the co-op to purchase power from Bonneville Power Administration in the same manner as before. He stressed the importance of the legislation to avoid a huge increase in the cost of power for those who were in the old PP&L service area. This will give those people the opportunity, through the co-op, to buy from Bonneville Power co-op rates. He submitted a list of proponents and the points that they made in support of the bill.

EXHIBIT (tas39a01)

Proponents' Testimony: Mike Uda, Regulatory Attorney for Energy Northwest, Inc. the subsidiary of Flathead Electric Cooperative, testified in support of the bill. He described the reason for the merger was to eliminate duplication and current regulatory duties between a cooperative and a public utility. He noted that currently, Energy Northwest had to operate in both capacities. They had to comply with the requirements with cooperatives in terms of governance, compliance with lending guidelines from cooperative lending institutions, and at the same time meet the requirements of a public utility. He stated, if there was ever a case where regulation can kill - it is this kind of a situation. This bill will eliminate that anomaly. Originally, they attempted to get authority from the Public Service Commission to simply approve the assignment under the existing authority under Title 69. That is where this bill will reside, unlike the other bill which will be under Title 35. The purpose of filing that in the first place was to avoid having to come to the Legislature and get an amendment to the existing law to accommodate the merger between Flathead Electric Cooperative and E&I. Essentially, in September of this last year, the Public Service Commission's view was they could not approve the merger based on the current law. A notice of petition for judicial review was filed in Flathead County with the agreement of the Public Service Commission that action was staid and that is where it currently is. That case will be thrown out if either SB 446 or SB 325 is passed. Currently, there are a number of pressing obligations under existing law for the cooperative to act as a public utility. For example, under SB 390, they were one of the cooperatives elected to go to customer choice and there is an obligation to file a position plan. There are multiple other regulatory responsibilities in addition to dealing with this catastrophic energy supply situation for the members of both the Flathead Electric Cooperative and E&I, but in particular E&I because if E&I is not merged they lose the ability to become eligible to provide their own preference power, which is

currently the best priced power available for the region. The intent of this law is not to change anything in existing law. The main thing is to eliminate the regulatory duplication and to insure those do not continue into the future. There is very little purpose in overlapping regulation between the Public Service Commission and the board members of both Flathead and E&I. The intent of having cooperative management is to have elected members make decisions for the people of the cooperatives. They are essentially a parallel governing body to the Montana Public Service Commission. He distributed a fact sheet demonstrating issues, solutions and benefits.

EXHIBIT (tas39a02) He also passed out a letter from Commissioner Rowe who could not attend the hearing. **EXHIBIT (tas39a03) {Tape : 1; Side : A; Approx. Time Counter : 0 - 9.6}** Mr. Uda pointed out that because of the situation with the energy markets and the difficulty in obtaining a reasonably priced supply of electricity, the regulatory, accounting and electric supply staff at Flathead Electric Co-op are overtaxed and overworked. He urged the committee pass this bill to ease the situation on the co-ops and the rate payers. He said the amendment that was circulating attempts to bind representations that were made in 1998 when Flathead purchased Pacific Corp's service territory, transmission distribution facilities in Flathead Valley and the Libby area. He commented that the Commission, under SB 446, obtains authorization to impose whatever conditions it likes on approval of the merger. For that reason, the amendment is not necessary. Also, we have learned from SB 390, that it is dangerous to be too prescriptive when dealing with the future. We don't know what the future is going to bring. The amendment purports to say if somebody made a representation in a proceeding four years ago, irrespective of what their understanding was then, that you should continue to hold them to it, irrespective of how drastic circumstances have changed. It would be an error to lock past representations into perpetuity. Therefore, the amendment should be rejected. **{Tape : 1; Side : A; Approx. Time Counter : 9.6 - 13.5}**

Chris Byrd, President of the Board of Energy Northwest and member of Flathead Electric Co-op, testified in support of the bill. He distributed written testimony. **EXHIBIT (tas39a04)**

Francis Rosse, Vice-President of the Board of Energy Northwest and member of Flathead Electric Cooperative, testified in support of the bill. He presented written testimony. **EXHIBIT (tas39a05) {Tape : 1; Side : A; Approx. Time Counter : 18.9 - 24}**

Joe Unterreine, Kalispell Chamber of Commerce, testified in support of the bill. He stressed the high concern of businesses in Flathead County regarding the impact of the high energy costs.

The Columbia Falls Aluminum Company has announced cutbacks. There is great concern with the operations of the Plum Creek Timber Company. This bill is highly supported by businesses in the Flathead area as it will create efficiencies. He noted the greatest concern was for energy and the costs of regulation, that if this is carried out, it would even result in a disincentive to be part of the city. **{Tape : 1; Side : A; Approx. Time Counter : 24 - 27}**

Warren McConkey, General Manager of Flathead Electric Cooperative and Energy Northwest, Inc., testified in favor of the bill. He said the bill would clarify the authorization for the Public Service Commission to consider a territorial assignment agreement to allow the complete merger of an acquired urban service area into an electric cooperative. The Bonneville Power Administration's denial to provide power at previous rates means an enormous economic impact on the Flathead Valley. The current market prices mean a \$9 million dollar a year impact on 13,000 customers. That is an enormous rate increase on that customer base. It is important to get the lowest cost power possible in Montana. He clarified that both Flathead Electric and Energy Northwest are currently not-for-profit corporations. Therefore, the consolidation would have no effect on income taxes. **{Tape : 1; Side : A; Approx. Time Counter : 27 - 30.7}** They have agreed to match property taxes to the Pacific Corp rate before the acquisition. That is by contract with the County Commissioners, for both rural and urban areas of the acquisition. He noted that 2,800 of their members had supported the consolidation and 30 had opposed it. He described reasons for the opposition and board regulation activity. He pointed out one situation was the pole attachment rates. Telecommunications and cable TV providers attached their cables to the poles. For that, they pay a rental fee on an annualized basis for the use of the pole. The FCC formula is used as a basis for calculating the pole attachment rate. It is considerably more than it was ten or twenty years ago. There is escalation plus the FCC formula has changed. It has included items that it didn't include before. A new pole attachment rate was implemented in early 2000. AT&T, doing business in Montana as TCI Cablevision, filed an official complaint. He distributed the ruling from that action. **EXHIBIT (tas39a06)** He read a paragraph from that ruling that described the essence of this situation and local regulation and how it worked, which was paragraph 2. **{Tape : 1; Side : B; Approx. Time Counter : 0 - 4.5}**

Opponents' Testimony: **Tom Harrison**, representing Spring Creek Coal, testified against the bill. He distributed an amendment that would make the bill satisfactory. **EXHIBIT (tas39a07)** He felt this bill did not add anything to SB 325, regarding the merger.

However, the concern is in subsection 3 of the new language. This section does not give the PSC Commission the authority to regulate a rural electric cooperative in any manner, other than to review the agreement. That can put conditions on the agreement, from now on. He described an example where lines could be built connecting other providers, then the PSC could approve it as far as the public interest was concerned. The bill, however, says once it is approved on the public interest issue, there is no way to enforce what they said they would do. The purpose of the amendment is to say they will review the agreement for being in the public interest, but then whatever the buyer and the seller of that area represent to the commission, the commission gets to see that they will carry it out. Presently, it is only applicable to the one area, which is the sale that took place a couple years ago from Pacific Corp to Flathead. The question is whether the representations that were made to the PSC, in which are still contained in the PSC order, are these, as a matter of public policy - to be lifted, saying the PSC has no power. He described the restrictions from the docket that they are operating under. They must adhere to the rate moratorium. Flathead must file a transition plan, they must not assess any customer in the service area a transition charge and must honor all contracts of Pacific Corp. All of those things were represented and considered by the commission in approving this sale. Now the question is whether the Legislature disregards this PSC ruling. Any future agreement can include adhering to a rate moratorium and other conditions. They sold the PSC on this idea, making these representations. This bill is just the elimination of any regulation by the PSC to make them do what they said they would do. **{Tape : 1; Side : B; Approx. Time Counter : 4.5 - 13.8}**

Questions from Committee Members and Responses: **SENATOR BOHLINGER** asked about the need for regulation and the continuation of the contractual agreement and whether this amendment would accomplish this. **Mr. Harrison** said that it did conceptually.

SENATOR BOHLINGER asked about the need for regulatory oversight. **Mr. McConkey** said this was a concern. The board of directors is elected from the citizenship to be the local regulatory authority of the day to day business of the cooperative. That does live up to their obligations, such as system reliability as a condition of the sale. Local regulation works and there are appeal processes for those that might be disgruntled. **{Tape : 1; Side : B; Approx. Time Counter : 13.8 - 18.2}**

SENATOR COLE asked for an update regarding the Decker Mine rates. **Mr. McConkey** replied the same rates would be a board determination. He pointed out the mines were already members of

Flathead Electric. They have since put out a bid to 15 power suppliers to approach a less than market purchase price. The mines are working with this on a daily basis. They have also approached the Tongue River Co-op for their assistance. Decker Coal Company said they had a power supply available if they could take delivery right at the border of Montana and own the entire distribution system. Flathead Electric said they would accommodate that as expeditiously as possible, as either a lease or sale. **SENATOR COLE** said the amendment would be appropriate to make sure everyone was treated equally. **Mr. McConkey** pointed out that cooperatives distributed power to their members on a cost basis. The cost of acquisition of power is part of that cost basis. When there is a rate class of customers that imposes a unique cost of service on the cooperative, the retail rates are composed of the distribution costs, transmission costs, administrative costs and the power supply costs all added together. When there is a unique power supply for a subset of the co-op members, then that power supply cost is added into that customers retail cost of service rate. They are not marked up, there is no profit, there is no margins on power supply. They are directly passed through. Spring Creek and Decker's tariff states clearly that the transmission cost and wholesale power costs are directly passed through at cost. It is not an averaged cost, partially because in the Flathead Valley there is primarily Bonneville Administration power, which by law they cannot deliver to a customer beyond 75 miles East of the Continental Divide. That is the Bonneville Project Act that preference based power can't be sold beyond that 75 mile zone. The power being sold to central Montana is surplus power, not the cost based power.

{Tape : 1; Side : B; Approx. Time Counter : 18.2 - 21.9}

SENATOR STONINGTON asked about PSC controls. **Mr. Uda** said they would be able to review transactions and impose conditions. This clarifies that the PSC cannot continue to have rate regulations over cooperatives. The idea is to get away from overlapping regulation. **{Tape : 2; Side : A; Approx. Time Counter : 0 - 5.2}**

VICE CHAIRMAN ELLIS said that contract law says that anything that is written between a server and a customer has to be followed if the server sells their business, such as the contract between Pacific Corp and Spring Creek or Decker. **Mr. Uda** replied yes the obligation is ongoing. Nothing in this bill affects any of those obligations. He noted the unintended consequences of SB 390. He gave some background information. He said essentially what happened is the border loads were Wyoming customers as of the day of the acquisition. As part of their agreement, they assumed the contracts of Pacific Corp including the contracts that serviced the mines. Currently, the problem they have is those contracts are expiring and there are no alternatives

available at the same price. They attempted to come up with a legal way of returning them to Wyoming service. For fiscal year 2001, the E&I and Flathead combined systems are already \$2 million dollars in the hole in power purchase costs. They are already looking at substantial rate increases. They are very sympathetic to the plight of the mines and are trying to help them in any way possible. They will continue to adhere to their responsibilities. The way in which those obligations were transferred, under SB 390 and Chapter 69, Title H, is that the rate moratorium that was applied to Pacific Corp as a utility, was not necessarily applied to a cooperative. It added ambiguity to the statute. A parallel producer applied as a cooperative and announced their intention to go to choice, as Flathead Electric Cooperative has, but it did not contain the rate moratorium provision. There is no clear guidance on this issue. However, there are exceptions under the law that say if you experience a power supply cost greater than 80% between July 1 of 2000 and June 30 of 2002, there an exception to the rate moratorium. He stated they were looking now at a 500% rate increase. At the recent PSC meeting, there was a one year offer from Pacific Corp to serve 70 megawatts of their base load resource. That was \$275 a megawatt hour. That would be about 6-7 times what Decker and Spring Creek are currently paying. He said he believed they qualified for those exemptions now and were committed to solve the problem any way they can. **{Tape : 2; Side : A; Approx. Time Counter : 5.2 - 11.3}**

VICE CHAIRMAN ELLIS asked if Wyoming PSC knew of this situation. **Mr. Uda** said the Montana Public Service Commission had approved the transfer of the jurisdictional assets in Montana to Flathead Electric. He was not sure what happened in Wyoming. This transfer occurred in November 1998. **SENATOR ELLIS** pointed out that the mines purchased power from the cooperative and at that time they had the option to purchase power for five years, three years or one year. The problem they faced is they chose, even though they didn't choose to be deregulated, they chose the wrong option as far as cost of power. **Mr. Uda** responded that they had made a decision and it turned out to be a bad one and so did a lot of other people. They did not know what the market was going to look like. **Mr. Harrison** spoke up that specifically the mines were part of the obligations of Flathead to provide the rates to. Under the moratorium, Flathead would not provide that rate. They said, at the time of the sale, that it was a seamless sale and they were under the moratorium so there would be no problem. The mines did not protest or appear before the PSC because they thought they were under the rate cap. They come back four months later and said things have changed and they could not service the mines at all. He noted that other companies, such as MRI, went

with the short term contracts. However, Spring Creek never opted out. **{Tape : 2; Side : A; Approx. Time Counter : 11.3 - 16}**

Closing by Sponsor: SENATOR DEPRATU closed. This legislation is an enabling bill for a serious situation in the Kalispell area. He suggested the amendment not be added. The bill would help up to a \$9 million dollar rate increase for 13,000 customers in the Kalispell area.

ADJOURNMENT

Adjournment: 9:25 A.M.

SEN. BOB DEPRATU, Chairman

DEB THOMPSON, Secretary

BD/DT

EXHIBIT (tas39aad)